

## **NORTH LINCOLNSHIRE COUNCIL**

### **AUDIT COMMITTEE**

#### **INTERNAL AUDIT – EFFECTIVENESS REPORT 2011/12**

##### **1. OBJECT AND KEY POINTS IN THIS REPORT**

- 1.1 To provide an opinion on the effectiveness of internal audit in accordance with the Accounts and Audit Regulations and CIPFA Code of Practice.
- 1.2 The assessment is based on the following:
- External Audit's assessment of Internal Audit's work
  - Compliance with Best Practice as defined by The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice for Internal Audit and Statement on the Role of the Head of Internal Audit
  - Customer feedback and endorsement
  - Achievement of performance targets.

##### **2. BACKGROUND INFORMATION**

- 2.1 Regulation 6 of the Accounts and Audit Regulations 2011 require an annual review of the effectiveness of Internal Audit as part of the consideration of the system of internal control. The need for the review is to ensure the opinion in Internal Audit's annual report can be relied on as an important source of assurance in support of the Annual Governance Statement.
- 2.2 The Regulation requires that adequate and effective internal audit of its accounting records and its system of internal control is maintained in accordance with proper internal audit practice.
- 2.3 The assessment is based on the following:
- External Audit's assessment of Internal Audit's work
  - Compliance with Best Practice as defined by CIPFA's Code of Practice for Internal Audit and Statement on the Role of the Head of Internal Audit
  - Customer feedback
  - Achievement of performance targets

- 2.4 External Audit previously undertook a full review of internal audit every three years and provided an assessment of compliance with the Code. The last review of the internal audit function was reported to the Audit Committee in June 2009. The review concluded that the internal audit function meets all 11 standards as set out within the CIPFA Code and that External Audit could rely on the work of Internal Audit to discharge their own audit responsibilities.

There have been no major changes to working practices since this time and regular self-assessments show that the section continues to meet the requirements of the Code of Practice.

External audit have continued to rely upon Internal Audit's work during 2011/12 as part of the audit of the council's financial statements.

- 2.5 Whilst adherence to the standards in the Code evidences professional competence and sound process, the Code also recognized that to be 'effective' internal audit should:

- Understand the whole council, its needs and priorities
- Understand its position with respect to the council's other sources of assurance and plan its work accordingly
- Be seen as a catalyst for change at the heart of the council
- Add value and assist the council in achieving its priorities
- Be forward thinking
- Be innovative and challenging
- Help to shape the ethics and standards of the council
- Ensure the right resources are available
- Share best practice with other auditors
- Seek opportunities for joint working with other auditors.

Appendix A shows how these issues have been addressed.

- 2.6 It is important to receive feedback on our work. Questionnaires are issued with each system review and establishment audit. Service managers are asked to comment on their satisfaction and value added from the audit work. All comments are appreciated and are used to improve our service delivery. One hundred percent of questionnaires returned considered the conduct, manner and attitude of the staff good or excellent.

- 2.7 The Internal Audit section constantly strives to improve the service they provide. There is a suite of performance measures and development issues set to monitor performance, set targets for improvements and provide comparison both internally and externally. The Section also participates in national and local benchmarking exercises. Overall performance improved during 2011/12 and targets were met. Details are provided below:

- 86% of the audit plan was achieved (target 80%), the shortfall being due a higher than anticipated level of unforeseen audit work. This is an improvement on last year (85%).
- Follow up work confirmed acceptable progress on implementation of agreed audit recommendations (67%, which is slightly, lower than last year – 69%) (although high risk areas receive closer attention).
- All customers were surveyed and quality control questionnaires returned showed 100% satisfaction with the service provided (target 80%).
- 74% of audits were completed within agreed allocations (76% last year). Although the target was met (70%) this indicator was adversely affected by the level of unforeseen work necessary during the year (details are provided in the Internal Audit Annual Report 2011/12).
- 98% of audits were reviewed by the supervisor within the timescale target of 70% compared with 81% last year.
- There was a significant improvement in the timeliness of the completion of audits within agreed timescales. The result rose to 74% from 59% last year (against a target of 70%).

2.8 Annual CIPFA benchmarking results were used to determine audit's VFM profile for 2011/12. Key cost comparisons used were:

- Cost per chargeable day: 6 lowest out of 69 authorities
- Cost per auditor: 8 lowest out of 69 authorities.

The cost comparisons were assessed against key performance outcomes and the service was evaluated as providing value for money (low cost/ high performance).

2.9 In January 2011 CIPFA issued the Statement on the Role of the Head of Internal Audit. The Statement is not mandatory but sets out what CIPFA considers best practice for Heads of Internal Audit. It sets out principles that define the core activities and behaviours that belong to the role of the Head of Internal Audit in public service organisations CIPFA recommends that organisations should use the Statement as the framework to assess their existing arrangements. An assessment was first carried out and reported to Members in September 2011 and indicated a significant level of compliance. The evaluation identified two areas for improvement to current arrangements:

- Decision making report checklist to include specific reference to audit advice on internal control issues. (This forms part of the review mentioned in the Risk Management Progress Report concerned with ensuring risk and other areas are properly considered in Cabinet and Cabinet Member reports).
- Liaison with external inspectors and review agencies should extend beyond external audit where appropriate when drawing up the internal audit strategy.

The updated assessment is summarised in appendix B.

2.10 The 2011/12 audit plan work was managed using audit management software. Some benefits the software has introduced include:

- Integrated time recording and audit planning modules
- Electronic working papers
- Automated recommendation tracking
- Automated performance management information.

2.11 Based on the findings described in the above paragraphs Internal Audit is assessed as providing an effective service to the council.

### 3. **OPTIONS FOR CONSIDERATION**

3.1 Internal Audit provides an important source of assurance on the adequacy of internal control throughout the council. Members should seek clarification on its contents as necessary to ensure Internal Audit's work was carried out in such a way to provide sufficient assurance to fulfil their role as set out in the Committee's terms of reference.

3.2 The Audit Committee may conclude Internal Audit's work was not carried out in an effective way and therefore cannot be relied upon as a source of assurance to fulfil its terms of reference.

### 4. **ANALYSIS OF OPTIONS**

4.1 It is a statutory requirement for the council to maintain an internal audit function and for its effectiveness to be reviewed on an annual basis. The information contained within this report provides evidence of that review and sets out the reasons for determining that the service provided by Internal Audit has been effective during 2011/12. In addition to the internal review, the External Audit work indicated that all of the standards set out in the CIPFA Code of Practice for Internal Audit had been met. This means that Internal Audit's work can be relied upon to provide an important source of assurance on the adequacy of the council's internal control environment. This report together with the Annual Internal Audit Report this report provides important reassurance that the council's governance processes are sound.

4.2 If the Committee concludes Internal Audit's work cannot be relied upon then an important source of assurance to enable them to fulfill their role is no longer available.

### 5. **RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)**

5.1 The work of the internal audit section enhances control over the use of the council's resources through the recommendations made in audit reports.

5.2 There are no additional staffing, property or IT implications

6. **OTHER IMPLICATIONS (STATUTORY, ENVIRONMENTAL, DIVERSITY, SECTION 17 - CRIME AND DISORDER, RISK AND OTHER)**

6.1 The requirement for an internal audit function is set out in the Accounts and Audit Regulations 2011. Internal audit will continue to assist the Chief Financial Officer discharge his statutory duty under the provisions of the Local Government Act 1972. The Accounts and Audit (Amendment) (England) Regulations 2011 require an annual review of the effectiveness of internal audit.

6.2 The effectiveness of internal audit's work is an important component of the Annual Governance Statement and promotes good corporate governance.

7. **OUTCOMES OF CONSULTATION**

7.1 The approach adopted to measure the effectiveness of internal audit has been agreed with external audit. Consultation takes place at all stages of audit work to ensure service provision is of a high standard. Customers are also invited to feedback on individual audit assignments to improve service delivery.

8. **RECOMMENDATION**

8.1 That the Audit Committee considers the effectiveness of Internal Audit in 2011/12 and the assurance provided on the adequacy as a key component of the council's internal review processes and internal control environment.

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**Background Papers used in the preparation of this report**  
**Audit Commission – Review of Internal Audit – June 2009**  
**CIPFA Role of Head of Internal Audit**  
**CIPFA Code of Practice for Internal Audit in the UK**

**Characteristics of Effectiveness**

<b>Characteristic</b>	<b>Arrangements in place</b>
Understand the whole council, its needs and priorities	The audit plan is prepared in consultation with Directors and key staff to ensure it meets the needs of the council. The scope of each audit assignment is discussed at the start to understand the risks and assurance required. Audit plan progress is discussed during the year to ensure the continued alignment of the audit plan and organisational needs.
Understand its position with respect to the council's other sources of assurance and plan its work accordingly	The audit plan is discussed with external audit to avoid duplication and maximise the total audit resources available. Other sources of assurance such as external inspections are identified at audit planning meetings with Directors.
Be seen as a catalyst for change at the heart of the council And Add value and assist the council in achieving its priorities	Internal audit provides assurance to Members and management on the effectiveness of the council's control environment comprising of risk management, control and governance. The work not only provides assurance but also identifies potential improvement in controls, changes to policies and value for money opportunities. During 2011/12 internal audit identified savings totalling £63k as a result of their work.
Be forward thinking and innovative and challenging	National and local issues are considered in developing the audit plan. New and emerging risks alongside service developments are incorporated during the year. The audit strategy has improved considerably in the last couple of years to a wider risk based approach incorporating both financial and none financial systems. This approach is regarded as good practice and is being adopted by other audit teams. Audit staff have access to relevant training, publications and websites to remain up to date on current audit and wider local government issues. Audit has provided specific training and information to raise awareness on counter fraud arrangements. This includes regular newsletters containing fraud alerts on new and emerging fraud risks. Different methods are used

	including elearning options – this was used to provide widespread information on the Bribery Act (the Police Authority is interested in adopting a similar approach).
Help to shape the ethics and standards of the council	Audit provides advice and support on new projects and significant system changes. An important aspect of the work is to help to ‘design out fraud’ in system changes. The audit plan includes key audits designed to provide assurance on the adequacy of corporate governance arrangements in place. The Code of Practice places ethical responsibilities on internal audit to ensure the independence and integrity of their work. For example, an annual declaration of interests is made by all staff and CRB clearance is obtained where appropriate prior to accessing certain personal records.
Ensure the right resources are available	The level of resources required, skilled mix and specialist knowledge or experience needed to deliver the audit plan is considered within the audit strategy each year. All staff are suitably qualified (Association of Accounting Technicians - AAT). Three members of the team are also professionally qualified (Chartered Institute of Public Finance and Accountancy – CIPFA). Training needs are assessed at annual employee development reviews (EDRs) and monitored through quarterly one to one meetings.
Share best practice with other auditors	The Head of Audit, Risk and Insurance regularly attends the regional Chief Internal Auditors Group which discusses issues affecting internal audit in local government and the wider public sector and shares instances of good practice. The council is also members of the CIPFA Better Governance Forum and Technical Information Service (TIS online) which are networks that provide best practice, guidance and training on current issues.
Seek opportunities for joint working with other auditors	Joint working has been explored with other audit teams to share specialisms and relevant experience. Audit reviews have been carried out on systems where two parties have an interest and assurance is provided to the other party.

<b>Head of Internal Audit Statement Principles</b>	<b>Core HIA responsibilities</b>	<b>Non-Compliance / Areas for Improvement</b>
<p>The HIA in a public service organisation plays a critical role in delivering the organisation's strategic objectives by championing best practice in governance, objectively assessing the adequacy of governance and management of existing risks, commenting on responses to emerging risks and proposed developments.</p>	<p>Helping to promote the benefits of good governance throughout the organisation.</p> <p>Working with others in the organisation who have a responsibility for promoting good governance.</p> <p>Giving advice to the Leadership Team and others on the control arrangements and risks relating to proposed policies, programmes and projects.</p> <p>Promoting the highest standards of ethics and standards across the organisation based on the principles of integrity, objectivity, competence and confidentiality.</p> <p>Demonstrating the benefits of good governance for effective public service delivery and how the HIA can help.</p> <p>Offering consultancy advice where the HIA considers that it is appropriate, drawing up clear terms of reference for such assignments.</p>	<p>Decision making report checklist to include specific reference to IA advice</p>
<p>The HIA in a public service organisation plays a critical role in delivering the organisation's strategic objectives by giving an objective and evidence based opinion on all aspects of governance, risk management and internal control.</p>	<p>Giving assurance on the control environment. This includes risk and information management and internal controls across all systems.</p> <p>Reviewing the adequacy of key corporate arrangements including eg risk strategy, risk register, anti fraud and corruption strategy, corporate plan.</p> <p>Producing an evidence based annual internal audit opinion on the organisation's control environment.</p> <p>Working closely with others to ensure that sufficient and relevant evidence is used. Where relying on others, clarifying the degree and basis for the reliance.</p>	



	<p>Reviewing significant partnership arrangements and major services provided by third parties and the controls in place to promote and protect the organisation's interests. Assessing whether lines of responsibility and assurance are clear.</p> <p>Liaising closely with the external auditor to share knowledge and to use audit resources most effectively.</p> <p>Producing an internal audit strategy that fits with and supports the organisation's objectives.</p> <p>Reviewing the organisation's risk maturity (including the organisation's own assessment) and reflecting this in the strategy.</p> <p>Consulting stakeholders, including senior managers and non-executive directors/elected representatives on the internal audit strategy.</p> <p>Setting out how the HIA plans to rely on others for assurance on the organisation's controls and risks and taking account of any limitations in assurance given by others.</p> <p>Liaising with external inspectors and review agencies where appropriate when drawing up the internal audit strategy.</p> <p>Liaising with the external auditor on the internal audit strategy, but not being driven by external audit's own priorities</p>	<p>Liaison arrangements are restricted to external audit only</p>
<p>The HIA in a public service organisation must be a senior manager with regular and open engagement across the organisation, particularly with the Leadership Team and with the Audit Committee.</p>	<p>Escalating any concerns through the line manager, Chief Executive, Audit Committee and Leadership Team, legal officers, external auditor as appropriate.</p> <p>Supporting the Audit Committee in reviewing its own effectiveness and advising the Chair and line manager of any suggested improvements.</p>	

	<p>Consulting stakeholders, including senior managers and non-executive directors/elected representatives on the internal audit strategy</p>	
<p>The HIA in a public service organisation must lead and direct an internal audit service that is resourced to be fit for purpose.</p>	<p>Leading and directing the internal audit service so that it makes a full contribution to and meets the needs of the organisation and external stakeholders.</p> <p>Determining the resources, expertise, qualifications and systems for the internal audit service that are required to meet internal audit's objectives; using a full range of resourcing options including consultancy, working with others and buying in where appropriate.</p> <p>Informing the Leadership Team and Audit Committee if there are insufficient resources to carry out a satisfactory level of internal audit, and the consequence for the level of assurance that may be given.</p> <p>Implementing robust processes for recruitment of internal audit staff and/or the procurement of internal audit services from external suppliers.</p> <p>Ensuring that the professional and personal training needs for staff are assessed and seeing that these needs are met.</p> <p>Developing succession plans and helping staff with their career progression.</p> <p>Establishing a quality assurance and improvement programme that includes:</p> <ul style="list-style-type: none"> <li>– Ensuring that professional internal audit standards are complied with.</li> <li>– Reviewing the performance of internal audit and ensuring that the service provided is in line with the expectations and</li> </ul>	

	<p>needs of its stakeholders.</p> <ul style="list-style-type: none"> <li>– Providing an efficient and effective internal audit service – demonstrating this by agreeing key performance indicators and targets with the line manager and Audit Committee; annually reporting achievements against targets.</li> <li>– Putting in place adequate ongoing monitoring and periodic review of internal audit work and supervision and review of files, to ensure that audit plans, work and reports are evidence based and of good quality.</li> <li>– Ensuring that any internal auditors declare any interests that they have.</li> <li>– Seeking continuous improvement in the internal audit service.</li> </ul> <p>Keeping up to date with developments in governance, risk management, control and internal auditing, including networking with other HIAs and learning from them, implementing improvements where appropriate.</p> <p>Demonstrating how internal audit adds value to the organisation.</p>	
<p>The HIA in a public service organisation must be professionally qualified and suitably experienced</p>		